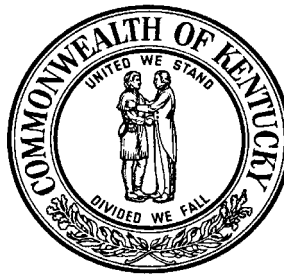


**REPORT OF THE AUDIT OF THE  
FORMER MAGOFFIN COUNTY  
SHERIFF'S SETTLEMENT - 2002 TAXES**

**January 5, 2003**



**EDWARD B. HATCHETT, JR.**  
**AUDITOR OF PUBLIC ACCOUNTS**  
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EDWARD B. HATCHETT, JR.  
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky

Honorable Paul E. Patton, Governor  
Gordon C. Duke, Secretary  
Finance and Administration Cabinet  
Dana Mayton, Secretary, Revenue Cabinet  
Honorable Bill W. May, Magoffin County Judge/Executive  
Honorable Pat Montgomery, Former Magoffin County Sheriff  
Honorable Randall Jordan, Magoffin County Sheriff  
Members of the Magoffin County Fiscal Court

The enclosed report prepared by Morgan-Franklin, LLC, Certified Public Accountants, presents the former Magoffin County Sheriff's Settlement - 2002 Taxes.

We engaged Morgan-Franklin, LLC, to perform the financial audit of this statement. We worked closely with the firm during our report review process; Morgan-Franklin, LLC, evaluated the former Magoffin County Sheriff's internal controls and compliance with applicable laws and regulations.

Respectfully submitted,

Edward B. Hatchett, Jr.  
Auditor of Public Accounts

Enclosure





**EXECUTIVE SUMMARY**

**AUDIT EXAMINATION OF THE  
FORMER MAGOFFIN COUNTY  
SHERIFF'S SETTLEMENT - 2002 TAXES**

**January 5, 2003**

Morgan-Franklin, LLC, has completed the audit of the Sheriff's Settlement - 2002 Taxes for the former Magoffin County Sheriff as of January 5, 2003. We have issued an unqualified opinion on the financial statement taken as a whole. Based upon the audit work performed, the financial statement is presented fairly in all material respects.

**Financial Condition:**

The former Sheriff collected taxes of \$1,462,651 for the districts for 2002 taxes, retaining commissions of \$61,241 to operate the former Sheriff's office. The former Sheriff distributed taxes of \$1,425,347 to the districts for 2002 Taxes. Taxes of \$12 are due to the districts from the former Sheriff and no refunds are due to the former Sheriff from the taxing districts.

**Report Comments:**

- The Former Sheriff Should Have Required The Depository Institution To Pledge Or Provide Additional Collateral, And Should Have Entered Into A Written Agreement To Protect Deposits
- The Former Sheriff's Office Lacked An Adequate Segregation Of Duties

**Deposits:**

The former Sheriff's deposits were not fully insured and collateralized by bank securities or bonds



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**Morgan-Franklin, LLC  
P.O. Box 428  
513 Main Street  
West Liberty, Kentucky 41472**

To the People of Kentucky

Honorable Paul E. Patton, Governor

Gordon C. Duke, Secretary

Finance and Administration Cabinet

Dana Mayton, Secretary, Revenue Cabinet

Honorable Bill W. May, Magoffin County Judge/Executive

Honorable Pat Montgomery, Former Magoffin County Sheriff

Honorable Randall Jordan, Magoffin County Sheriff

Members of the Magoffin County Fiscal Court

Independent Auditor's Report

We have audited the former Magoffin County Sheriff's Settlement - 2002 Taxes as of January 5, 2003. This tax settlement is the responsibility of the former Magoffin County Sheriff. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, and the Audit Guide for Sheriff's Tax Settlements issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the Sheriff's office prepares the financial statement on a prescribed basis of accounting that demonstrates compliance with the modified cash basis and laws of Kentucky, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the accompanying financial statement referred to above presents fairly, in all material respects, the former Magoffin County Sheriff's taxes charged, credited, and paid as of January 5, 2003 in conformity with the modified cash basis of accounting.

In accordance with Government Auditing Standards, we have also issued our report dated October 17, 2003, on our consideration of the former Sheriff's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

To the People of Kentucky

Honorable Paul E. Patton, Governor

Gordon C. Duke, Secretary

Finance and Administration Cabinet

Dana Mayton, Secretary, Revenue Cabinet

Honorable Bill W. May, Magoffin County Judge/Executive

Honorable Pat Montgomery, Former Magoffin County Sheriff

Honorable Randall Jordan, Magoffin County Sheriff

Members of the Magoffin County Fiscal Court

Based on the results of our audit, we present the accompanying comments and recommendations, included herein, which discuss the following report comments:

- The Former Sheriff Should Have Required The Depository Institution To Pledge Or Provide Additional Collateral, And Should Have Entered Into A Written Agreement To Protect Deposits
- The Former Sheriff's Office Lacked An Adequate Segregation Of Duties

Respectfully submitted,

*Morgan - Franklin, LLC*

Morgan-Franklin, LLC

Audit fieldwork completed -  
October 17, 2003

MAGOFFIN COUNTY  
PAT MONTGOMERY, FORMER MAGOFFIN COUNTY SHERIFF  
SHERIFF'S SETTLEMENT - 2002 TAXES

January 5, 2003

<u>Charges</u>	<u>County Taxes</u>	<u>Special Taxing Districts</u>	<u>School Taxes</u>	<u>State Taxes</u>
Real Estate	\$ 451,524	\$ 284,522	\$ 708,213	\$ 208,753
Tangible Personal Property	65,803	28,429	62,042	36,980
Intangible Personal Property				9,215
Fire Protection	2,971			
Increases Through Exonerations	78	49	123	36
Franchise Corporation	116,468	51,975	114,918	
Fire Protection	2,837			
Additional Billings	1,067	683	1,813	540
Adjusted to Sheriff's Receipt	<u>(3,019)</u>	<u>(15)</u>	<u>(67)</u>	<u>(16)</u>
Gross Chargeable to Sheriff	<u>\$ 637,729</u>	<u>\$ 365,643</u>	<u>\$ 887,042</u>	<u>\$ 255,508</u>
<u>Credits</u>				
Exonerations	2,811	1,763	4,386	1,312
Discounts	6,822	4,054	9,943	3,383
Tax Bills Transferred to Incoming Sheriff				
Real Estate	165,487	103,784	258,332	76,146
Tangible Personal Property	10,441	4,511	9,844	5,638
Intangible Personal Property				2,558
Uncollected Franchise	<u>3,888</u>	<u>2,359</u>	<u>5,811</u>	
Total Credits	<u>\$ 189,449</u>	<u>\$ 116,471</u>	<u>\$ 288,316</u>	<u>\$ 89,037</u>
Taxes Collected	\$ 448,280	\$ 249,172	\$ 598,726	\$ 166,471
Less: Commissions *	<u>19,339</u>	<u>10,590</u>	<u>23,949</u>	<u>7,363</u>
Taxes Due	\$ 428,941	\$ 238,582	\$ 574,777	\$ 159,108
Taxes Paid	428,942	238,576	598,722	159,107
Refund of School Commissions			<u>(23,949)</u>	
Due Districts as of		**		
Completion of Fieldwork	<u>\$ (1)</u>	<u>\$ 6</u>	<u>\$ 4</u>	<u>\$ 1</u>

\* and \*\* See Page 4.

The accompanying notes are an integral part of this financial statement.

MAGOFFIN COUNTY  
PAT MONTGOMERY, MAGOFFIN COUNTY SHERIFF  
SHERIFF'S SETTLEMENT - 2002 TAXES  
January 5, 2003  
(Continued)

\*Commissions:

10% on	\$	10,000
4.25% on	\$	853,923
4% on	\$	598,723

\*\*Special Taxing Districts:

Library District	\$	1
Extension District		2
Health District		1
Soil Conservation District		3

Due Districts or (Refunds Due Sheriff)	\$	<u>7</u>
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The accompanying notes are an integral part of this financial statement.

MAGOFFIN COUNTY  
NOTES TO FINANCIAL STATEMENTS

January 5, 2003

Note 1. Summary of Significant Accounting Policies

A. Fund Accounting

The Sheriff's office tax collection duties are limited to acting as an agent for assessed property owners and taxing districts. A fund is used to account for the collection and distribution of taxes. A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

B. Basis of Accounting

The financial statement has been prepared on a modified cash basis of accounting. Basis of accounting refers to when charges, credits, and taxes paid are reported in the settlement statement. It relates to the timing of measurements regardless of the measurement focus.

Charges are sources of revenue which are recognized in the tax period in which they become available and measurable. Credits are reductions of revenue which are recognized when there is proper authorization. Taxes paid are uses of revenue which are recognized when distributions are made to the taxing districts and others.

C. Cash and Investments

At the direction of the fiscal court, KRS 66.480 authorizes the Sheriff's office to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

Note 2. Deposits

The former Sheriff maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the Sheriff and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution. However, as of January 8, 2003, the collateral and FDIC insurance together did not equal or exceed the amount on deposit, leaving \$1,167,710 of public funds uninsured and unsecured. In addition, the former Sheriff did not have a written agreement with the depository institution securing the former Sheriff's interest in the collateral.

MARTIN COUNTY  
 NOTES TO FINANCIAL STATEMENT  
 January 5, 2003  
 (Continued)

Note 2. Deposits (Continued)

The county official's deposits are categorized below to give an indication of the level of risk assumed by the county official as of January 8, 2003.

	<u>Bank Balance</u>
FDIC insured	\$ 100,000
Collateralized with securities held by pledging depository institution in the county official's name	
Uncollateralized and uninsured	<u>1,167,710</u>
Total	<u><u>\$ 1,267,710</u></u>

Note 3. Tax Collection Period

Property Taxes

The real and personal property tax assessments were levied as of January 1, 2002. Property taxes were billed to finance governmental services for the year ended June 30, 2003. Liens are effective when the tax bills become delinquent. The collection period for these assessments was November 26, 2002 through January 5, 2003.

Note 4. Interest Income

The former Magoffin County Sheriff earned \$194 as interest income on 2002 taxes. The former Sheriff distributed the appropriate amount to the school district as required by statute, and the remainder was used to operate the Sheriff's office.

## COMMENTS AND RECOMMENDATIONS





MAGOFFIN COUNTY  
PAT MONTGOMERY, FORMER MAGOFFIN COUNTY SHERIFF  
COMMENTS AND RECOMMENDATIONS

As of January 5, 2003

STATE LAWS AND REGULATIONS:

The Former Sheriff Should Have Required The Depository Institution To Pledge Or Provide Additional Collateral, And Should Have Entered Into A Written Agreement To Protect Deposits

On January 8, 2003, \$1,167,710 of the former Sheriff's deposits of public funds were uninsured and unsecured. According to KRS 66.480(1)(d) and KRS 41.240(4), financial institutions maintaining deposits of public funds are required to pledge securities or provide surety bonds as collateral to secure these deposits if the amounts on deposit exceed the \$100,000 amount of insurance coverage provided by the Federal Deposit Insurance Corporation (FDIC). The former Sheriff should have required the depository institution to pledge or provide collateral in an amount sufficient to secure deposits of public funds at all times. We also recommend the Sheriff's office enter into a written agreement with the depository institution to secure the Sheriff's interest in the collateral pledged or provided by the depository institution. According to federal law, 12 U.S.C.A. § 1823(e), this agreement, in order to be recognized as valid by the FDIC, should be (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution.

*Former Sheriff Pat Montgomery's Response:*

*None.*

INTERNAL CONTROL - REPORTABLE CONDITIONS:

The Former Sheriff's Office Lacked An Adequate Segregation Of Duties

During our audit we noted the former Sheriff's internal control structure lacked an adequate segregation of duties. This deficiency occurs when someone has custody over assets and the responsibility of recording financial transactions. In our judgment, this condition could have adversely affected the former Sheriff's ability to record, process, summarize, and report accurate financial information. We recommend the Sheriff's office obtain additional staff to divide the responsibilities or implement the following compensating controls that would help offset the lack of adequate segregation of duties:

- Cash recounted and deposited by the Sheriff
- Reconciliation of reports to source documents and receipts and disbursements ledgers by the Sheriff
- All disbursement checks are to be signed by two people and one must be the Sheriff
- All disbursements checks prepared by an employee are examined by the Sheriff for proper documentation.
- The Sheriff mails disbursements
- The Sheriff or someone independent of the Sheriff's Office prepares bank reconciliations

*Former Sheriff Pat Montgomery's Response:*

*None.*

PRIOR YEAR:

*None.*

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REPORT ON COMPLIANCE  
AND ON INTERNAL CONTROL OVER FINANCIAL  
REPORTING BASED ON AN AUDIT OF THE FINANCIAL STATEMENT  
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS



**Morgan-Franklin, LLC**  
**P.O. Box 428**  
**513 Main Street**  
**West Liberty, Kentucky 41472**

To the People of Kentucky

Honorable Paul E. Patton, Governor  
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Honorable Randall Jordan, Magoffin County Sheriff  
Members of the Magoffin County Fiscal Court

Report On Compliance And On Internal Control  
Over Financial Reporting Based On An Audit Of The Financial  
Statement Performed In Accordance With Government Auditing Standards

We have audited the former Magoffin County Sheriff's Settlement - 2002 Taxes as of January 5, 2003, and have issued our report thereon dated October 17, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the former Magoffin County Sheriff's Settlement - 2002 Taxes as of January 5, 2003, is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance that is required to be reported under Government Auditing Standards, and which is described in the accompanying comments and recommendations.

- The Former Sheriff Should Have Required The Depository Institution To Pledge Or Provide Additional Collateral And Should Have Entered Into A Written Agreement To Protect Deposits

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the former Magoffin County Sheriff's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statement and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statement. The reportable condition is described in the accompanying comments and recommendations.

- The Former Sheriff's Office Lacked An Adequate Segregation Of Duties

Report On Compliance And On Internal Control  
Over Financial Reporting Based On An Audit Of The Financial  
Statement Performed In Accordance With Government Auditing Standards  
(Continued)

Internal Control Over Financial Reporting (Continued)

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statement being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we do not believe the reportable condition described above is a material weakness.

This report is intended solely for the information and use of management and is not intended to be and should not be used by anyone other than the specified party.

Respectfully submitted,

*Morgan - Franklin, LLC*

Morgan-Franklin, LLC

Audit fieldwork completed -  
October 17, 2003

